

## **An Incomplete List of Possible Progressive Reforms in Corporate Governance**

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### **1. Dismantle Shareholder Supremacy**

\* One version of the law now: “A [] corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end.” (Dodge).

\* Alternative version allows the board of directors to determine the purpose and interests of the corporation: “A corporation may be ... organized to conduct ... any lawful business or purposes” (Del 101); RMBCA § 8.30(a) (“Each member of the board of directors... shall act ... in a manner the director reasonably believes to be in the interests of the corporation”). In Delaware, these duties are separated into the duty of loyalty, namely the director’s obligation to act “in the good faith belief that her actions are in the corporation’s best interest,” *Guttman v. Huang*, 823 A.2d 492, 506 (Del. Ch.2003), see also, *In re Walt Disney Co.*, 2004 WL 2050138 (Del.Ch. 2004) (holding that the “duty of loyalty ... imposes an affirmative obligation to protect and advance the interests of the corporation and mandates that a director absolutely refrain from any conduct that would harm the corporation”), and the duty of care, namely the requirement that “in making business decisions, directors must consider all material information reasonably available,” *Brehm v. Eisner*, 746 A.2d 244, 259, 264 (Del. 2000) (also noting that Delaware duty of care is purely procedural). See also Del. Gen. Corp. L. § 145 (permitting indemnification of directors and others who act in “good faith and in a manner the person reasonably believed to be in or not opposed to the interests of the corporation”).

\* Only shareholders are permitted to vote for the board of directors, on an anti-democratic basis of one-share, one vote.

\* Only shareholders may sue to enforce directorial fiduciary obligations.

\* Most shareholders are institutions, managed by fiduciaries who are under intense market pressure to maximize the value of the shares they hold.

\* The richest 10% of Americans own 90% of stocks; the wealthiest 20% own 98%; shareholder supremacy thus is a policy that benefits the rich at the expense of other stakeholders (primarily workers).

\* Workers and other stakeholders are largely ignored in corporate law.

\* Minor change could occur through broadening fiduciary duties, but must be accompanied by new causes of action allowing non-shareholders to enforce duties or it will merely make shareholder-elected boards more autonomous or responsive to market pressures.

#### **1A. Recognize long-term dependence of employees on corporation by including them in governance**

\* Other countries require workers on boards of directors.

- \* Effective change would require that workers, and possibly other corporate constituencies, have the right to elect a specified minimum percentage of the members of the board of directors.

- \* Employees depend on the continued existence of their jobs and employer, both because of “firm-specific investment” (non-transferable skills and connections, seniority, etc) and because of non-transferable pensions and medical insurance.

- \* Because employees are the most affected and most dependent corporate constituency, they need special protection.

### **1B. Bring corporations into the democratic age by creating democratic voting for the board of directors**

- \* Currently only shares vote.

- \* Fiduciaries who vote shares ordinarily are required to consider only the interests of shares, not the full interests of the human beings behind the shares.

- \* Part of board should be elected by human beings affected by the corporation (employees, beneficial owners of shares, community) on a one person one vote basis

### **2. End Delaware’s Dominance**

- \* Delaware’s population is less than 1/3 of 1% of nation, but Delaware is the state of incorporation of more than 50% of U.S. public companies and more than 60% of the Fortune 500.

- \* 300 largest DE corporations employ over 15 million employees.

- \* E.g., Wal-Mart alone employs over 50% more people than live in Delaware.

- \* Change could come either by way of federalizing corporate charters or weakening the “internal affairs” doctrine. Any state could unilaterally choose to opt out of the Delaware system by abolishing “internal affairs” and applying ordinary choice of law rules to corporations doing business in its territory.

### **3. Pass Anti-Fraud Laws for Employees**

- \* We have a huge legal regime to protect shareholders from untruthfulness.

- \* No federal law makes it illegal for corporations to lie to employees.

- \* Truth is as least as important in the labor market as in the securities market.

- \* Any individual state could create a disclosure regime for employees, consumers or citizens, based on Blue Sky Laws or political contribution disclosure laws, requiring disclosure of (1) adequacy of pension funding, (2) lobbying expenses, (3) investments in maintaining, modernizing or replacing plant and technology.

### **4. Limit Limited Liability**

- \* LL increases incentives for risky behavior (moral hazard problem).

- \* LL effects transfer of wealth from victims of corporate torts to shareholders.

- \* Corps routinely organize themselves to isolate risky activities in wholly owned subsidiaries.

### **5. Link CEO Pay to Worker Pay**

- \* 20 years ago, pay for CEOs was less than 30 times the pay of average worker. Now, the typical CEO makes more than 400 times as much as the average (not lowest paid) worker.

- \* CEO compensation rose 600% between 1990 and 2000.
- \* CEO pensions are usually protected even when workers' plans fail.
- \* CEO pay could be capped at ratio to average or minimum worker pay.
- \* CEO pay could be capped at ratio to total domestic payroll, to provide incentives for creating good jobs.

- \* CEO pay over \$1million should be deemed a distribution of profits for tax purposes (i.e., not deductible to the corporation). Current law already restricts deductions to \$1 million salary but has a loophole allowing unlimited additional CEO pay so long as it is tied to stock price or performance.

- \* CEOs should be required to have same benefit plans (health, pension, etc) as rank and file.

- \* Large corporations could be required to disclose basic wage structures and other working conditions information, thereby improving employee bargaining abilities and exposing inequities.

## **6. Stop Corporate Illegalities**

- \* Conservative theorists argue that corporations should break the law if the "expected cost" is less than the "expected benefit" to the corporation (calculated only on the basis of private profit). Fishel and Easterbrook: "Managers have no general obligation to obey regulatory laws, when violations are profitable to the firm."

- \* By some accounts, corporate crime is on the rise.

- \* One idea: shareholder activists using ultra vires doctrine to enjoin corporate crime (but shareholders can only prevail if they can show financial damages in their role as shareholders)

- \* Give citizens a private right of action to recover damages caused to society as a whole by corporate illegality, with most recovery going to the state but some to the "private attorney general."

## **7. End Differences Between Tax Accounting and In-House Accounting**

- \* Corps issue dividends in years when they don't report profits for tax purposes.

- \* One idea: same profits must be reported to both shareholders and IRS.

- \* Weaker alternative: both sets of books must be made public to shareholders and employees, with an explanation of differences.

- \* Or, presumption of fraud if different profits are reported in different contexts.

## **8. Limit Corporate Intervention Into Political Affairs**

- \* Modern governments use regulation to assure that Adam Smith's invisible hand works to social benefit

- \* When corporations influence regulation, they enable the market to control politics instead of the other way around.

\* Corporate lobbying and electoral interventions could be deemed a breach of duty of legality, enforced by a citizen's action, or a misuse of corporate funds, enforceable by a shareholders' derivative action.

### **9. Limit mobility of capital to reduce capital's advantage in negotiations with labor and consumers**

- \* Stock and bond markets can move money instantaneously and internationally
- \* Full diversification makes stock portfolios act as if they were risk neutral or risk loving
- \* In contrast, employees are always restricted to particular places and times and less able to "walk" and therefore less able to win negotiations.
- \* Capital gains taxes reduce the mobility of capital and should be kept at levels at least as high as ordinary income.

### **10. Improve general wealth and welfare provisions**

- \* Market economies tend to increase inequality, since the rich are better able to hold out for a disproportionate share of the surplus to trade.
- \* Accordingly, decent legal systems must have provisions to counteract this, including

Effective corporate income tax.

Progressive income tax.

Wealth taxes, especially on inherited, unearned, wealth.

Higher taxes on unearned income.

Medical care and pension funds that are independent of particular employers, to increase employee mobility (and ability to bargain) and to protect against employer misuse of funds, funded by general tax revenues to avoid placing domestic firms at a competitive disadvantage with respect to overseas competitors.

High minimum wage indexed to inflation.

Well funded schools and skill training programs.

Tort liability for corporate torts based on a theory of enterprise liability rather than fictional assumptions that employees are not part of the corporation when they are involved in torts.

Strong limits on intervention of wealth into the political process, including limits on corporate campaign contributions and campaign and lobbying expenditures.